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RHEHNSC/NSC WASHDC
RUMIAAA/HQ USSOUTHCOM MIAMI FL
RUCPDO/DEPT OF COMMERCE
RUEATRS/DEPT OF TREASURY

C O N F I D E N T I A L CARACAS 002380

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HQ SOUTHCOM ALSO FOR POLAD
TREASURY FOR MMALLOY
NSC FOR JCARDENAS AND JSHRIER
COMMERCE FOR 4431/MAC/WH/MCAMERON

E.O. 12958: DECL: 12/29/2017
TAGS: [ECON](#) [EFIN](#) [PGOV](#) [VE](#)
SUBJECT: NEW BOLIVAR, SAME OLD ECONOMY

REF: A. CARACAS 2130

[1](#)B. CARACAS 2040
[1](#)C. CARACAS 568

Classified By: Economic Counselor Andrew N. Bowen for reasons 1.4 (b) a
nd (d).

[1](#)1. (C) Summary: The BRV is finalizing plans to change the denomination of its currency. Beginning January 1, 2008, one new bolivar (known during the transition period as the bolivar fuerte, or "strong" bolivar) will be worth 1000 old bolivars. Venezuela's Central Bank has provided what appears to be reasonably competent leadership to the redenomination process, undertaking a multifaceted public information campaign and coordinating with the financial sector through the Superintendency of Banks. Private banks appear prepared, although many local observers predict various degrees of confusion, anxiety, and/or fraud during the transition process. At this point there is no indication that the redenomination will be accompanied by significant macroeconomic policy changes. Many economists therefore question the need for the redenomination, noting that it will impose a one-time cost on the state and private sector without any appreciable economic benefits. End summary.

An Idea Takes Shape

[1](#)2. (SBU) President Chavez announced the BRV's plan for redenomination of the bolivar on February 16, 2007; a legal decree followed on March 6 (ref C). Chavez offered the following reasons for the plan: to propel the bolivar to recover ground against the dollar and other currencies; to make the payment system more efficient and simplify cash accounting; to instill confidence in the national currency and the nation's psyche; and to help reduce inflation to a single digit. As Chavez is well aware, many Venezuelans fondly remember the era in the mid to late 1970s when the exchange rate was stable at 4.3 bolivars (Bs)/USD; after the redenomination, the official exchange rate will change from 2150 Bs/USD to 2.15 Bs/USD.

[1](#)3. (C) According to the chief economist of a large Venezuelan bank, the idea for redenomination came from staff at Venezuela's Central Bank (BCV), who hoped that it might be

part of a broader set of anti-inflationary policies. BCV staff discussed the idea with the finance commission of the National Assembly, whose then-chair, Rodrigo Cabezas, planted the idea with Chavez. Cabezas, whom Chavez subsequently appointed as Finance Minister, has in recent months backed off somewhat from his initial public assertions that the redenomination was necessary to fight inflation. In a recent interview with daily El Nacional, Cabezas defended the redenomination as a way of closing a "cycle of price instability" and promised it would be accompanied by additional economic measures including enhanced fiscal responsibility, improvements in CADIVI (the agency that manages the BRV's exchange controls), and support for local production.

The Mechanics of the Conversion

¶4. (U) The BCV has developed and widely communicated a timeline for conversion to the new denomination. As of October 1, 2007, businesses were obliged to list prices in both current and new bolivars. The BCV head unveiled samples of the new bills and coins in a November press conference broadcast by "cadena" on all TV stations, and posters showing the new bills and coins are now widely available. As of January 1, 2008, all prices and bank deposits must be listed in new bolivars. Starting January 2, banks are obligated to make cash conversions from old to new bolivars free of charge to anyone who requests it (banks may place a limit based on quantity of new bolivars they have on hand; several bank presidents have told us they anticipate their initial supply of new bolivars will not cover all conversion requests). During the transition period, which will last at least six months, consumers may pay for purchases in any combination of old and new bolivars. After the transition period, the old bolivars will no longer be accepted as payment, although individuals will still be able to convert them to new bolivars.

¶5. (C) All presidents of private banks we have talked with have told us they will be ready for the conversion. They noted, however, that their management teams were stretched because of the short time frame and the concurrent imposition of the tax on financial transactions (ref A). Citibank Venezuela president Bernardo Chacin (strictly protect throughout) said that a team from the Superintendency of Banks was auditing individual banks to ensure their preparations were on track. He predicted that Citibank and other private banks would be ready, but questioned whether public banks and the BCV would be. Banco Venezolano de Credito president Oscar Garcia Mendoza (strictly protect throughout) also questioned whether the BCV would be ready, specifically in terms of their capacity to safeguard the large quantities of bills in circulation and to destroy the old bills as they received them from banks. He said that BCV staff had sent a memo to BCV administrators claiming that the BCV did not have the capacity to prepare for the transition in the allotted timeframe.

¶6. (C) Several banking sector contacts have mentioned concern over the potential for money laundering during the reconversion. They note that banks will be required to convert potentially large amounts of cash for people who are not regular customers. Pedro Almoguera (strictly protect), Technical Executive Director of the Venezuelan Banking Association, told econoff that after some deliberation the BRV and the banks had concluded that no additional safeguards were necessary for converting large amounts of old to new bolivars in cash, as the individual in question would have the same value of cash in hand before and after the transaction. Should the individual then try to deposit the cash into an account, he continued, existing safeguards would apply.

The Bottom Line: Some Confusion and No Real Impact

¶17. (C) Most contacts believe there will be some degree of confusion, anxiety, and fraud during the transition period, although there they differ on the exact nature and extent of the problems. Some, like Garcia Mendoza, believe that many people who do not understand what the conversion means will be shocked to see their bank accounts or paychecks apparently reduced by a factor of 1000. Others, like Chacin, foresee increased fraud, as unscrupulous individuals take advantage of initial confusion to charge customers the same quantity of new bolivars that the item used to cost in old bolivars, to raise prices, or to refuse to provide change. A number of contacts expressed concern over the potential for counterfeiting, especially given the BRV's inadequate legal framework. (Note: As one lawyer explained it to us, a 2001 law, by negating several older laws, changed counterfeiting from a crime to an administrative offense, thus considerably reducing the deterrent to counterfeiting. End note.) Overall, however, most observers believe that whatever problems arise will work themselves out over the course of the transition period.

¶18. (SBU) More fundamentally, economists note that redenomination per se will have no impact on Venezuela's economy. Despite Cabezas' assertion that additional economic measures would accompany the redenomination, none of our contacts believe the government has a coherent plan to tackle inflation, reduce the distortions created by exchange controls and an overvalued official exchange rate, or increase domestic productivity. Although many see the redenomination as an ideal time to devalue the bolivar, Cabezas has publicly emphasized that there will be no devaluation in 2008 (ref B). (Note: One analyst thinks there is a small chance that the government might actually appreciate the bolivar to 2 Bs/USD on January 1, 2008. Separately, recent statements by Cabezas indicate that the BRV is reviewing its price control regime, reported septel. End note.) Estimates we have seen for the one-time cost of redenomination are in the range of USD 350 to 400 million for the BRV and roughly the equivalent amount for the private sector. Many of our contacts question the wisdom of the redenomination, given its cost and likely negligible economic impact.

Comment

¶19. (C) If unaccompanied by other measures, the redenomination will have little economic significance. Instead, it will be the subject of a struggle between the government and opposition economists over framing. The BRV will continue to depict redenomination as a measure to strengthen Venezuela following the slogan "a strong economy, a strong bolivar, a strong country." Opposition economists and commentators will highlight whatever problems arise during the transition process and point out that redenomination will not help address the country's real economic problems such as inflation and scarcity. In our estimation, the BRV has more to lose than to gain from redenomination: Venezuelans will not see any improvements in their lives, and whatever hassles and problems that arise during the transition period will contribute to increasing frustration over economic problems. End comment.
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